HM TREASURY

Special Resolution Regime:

the draft FSMA (Contribution to Costs of Special Resolution Regime) Regulations 2010

March 2010

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1 Introduction

1.1 The Financial Services Compensation Scheme (FSCS) is the scheme established by the Financial Services Authority (FSA) to compensate customers of authorised financial services firms when those firms are in default (i.e. unable, or likely to be unable, to satisfy claims against them). The Banking Act 2009 inserted a new section 214B into the Financial Services and Markets Act 2000 (FSMA), which made provision to allow the Treasury to require the FSCS to contribute to the cost of using the special resolution regime to resolve a failing bank or building society. This contribution would be limited to the amount that the FSCS would have had to pay out in respect of the failed bank if it had instead gone into default without any Government intervention.

The existing regulations and consultation

1.2 The Treasury made the FSMA (Contribution to Costs of Special Resolution Regime) Regulations 2009[1] (the "2009 Regulations") on 29 March 2009 in order to be able to require the FSCS to contribute towards the costs of the resolution of the Dunfermline Building Society (DBS) using the special resolution regime (SRR) powers in Part 1 of the Banking Act 2009. As a result, it was not possible to consult on draft regulations before they were made. Following a notification under those regulations, the FSCS will be required to make a contribution to the DBS resolution costs at the end of the resolution process. The regulations were approved by Parliament under the made affirmative procedure on 5 May and 6 May. The 2009 Regulations are available on the OPSI website.[2]

1.3 From 21 July – 31 October 2009, the Government consulted on the 2009 Regulations and sought views on a number of points that had come to the Treasury's attention since those regulations were made.[3] The results of the consultation are discussed in Chapter 2. Respondents to the consultation emphasised the importance of controlling the costs incurred in a bank resolution that are to be met by the FSCS, and the accountability of the resolution authorities in incurring these costs. One respondent expressed the view that the SRR costs to which the FSCS can be required to contribute should be limited to those costs associated with the compensation of depositors.

1.4 The Government appreciates the concerns of industry about control and accountability of the costs incurred in a bank resolution, and recognises the economic interest that the industry has in the outcome of any resolution. Having considered the responses, the Government remains of the view that the principles underlying the existing regulations are appropriate.

[1] S.I. 2009/807.

[2] www.opsi.gov.uk.

[3] The consultation document Special resolution regime: the FSMA (Contribution to Costs of Special Resolution Regime) Regulations 2009 and consultation responses, are available from the consultations and legislation section of the HM Treasury website, www.hm-treasury.gov.uk.

Further changes included in the Financial Services Bill

1.5 Subject to Parliamentary approval, the Financial Services Bill (which was introduced in the House of Commons on 19 November 2009) will make significant corrections to the provisions introduced into FSMA by the Banking Act 2009. These ensure that the limit on the costs charged to the FSCS reflect the true amount that the FSCS would have had to pay out if the failed bank had become insolvent. Section 214B is revoked and replaced by new sections 214B, 214C and 214D. These also restate the existing section 214B provisions more clearly and make some other minor technical changes and improvements. The two key changes are:

- the Government will be able to include the interest costs that it or another authority has borne in funding the resolution, in calculating the net cost of the resolution to which the FSCS would be required to contribute; and
- the maximum contribution the FSCS can be required to make will include the interest costs that the FSCS would itself have borne if it had needed to fund compensation payments to depositors and other claimants of the failed firm.

1.6 These measures will bring the calculation of FSCS contributions to SRR costs in line with normal commercial and Government practice. The changes will be effective from 19 November 2009 – the day that the Financial Services Bill was introduced into Parliament. This means that interest arising after 19 November can be included in the calculation of the costs arising from the DBS resolution, and in the calculation of the limit on FSCS contributions applicable to that resolution.

Consultation and impact assessment

1.7 This consultation seeks views on all aspects of the draft FSMA (Contribution to Costs of Special Resolution Regime) Regulations 2010 ("the draft 2010 Regulations") which will be made under the new FSMA provisions when clause 28 of the Financial Services Bill is enacted. The draft 2010 Regulations are available from the legislation and consultations section of the Treasury website. A summary of the regulations is given in Chapter 3.

1.8 An assessment of the effect of the policy changes made by the new sections 214B, 214C and 214D FSMA was included in the Financial Services Bill impact assessment.[4] There have been no significant changes to the proposals since that impact assessment was published and the relevant section ("Impact Assessment of allowing the cost of funding the exercise of SRR powers to be recovered from the FSCS") is included in this consultation document.

[4] Available on the Treasury website (www.hm-treasury.gov.uk).

2 Consultation responses

2.1 From 21 July – 31 October 2009, the Government consulted on the 2009 Regulations and sought views on a number of points that had come to the Treasury's attention since those regulations were made. A summary of respondent's views on each consultation question is set out below, together with the Government's response.

Q1 – What are your views on the costs to which the FSCS can be required to contribute?

2.2 Most respondents did not focus in detail on the specific question of the costs to which the FSCS should be required to contribute. Instead they emphasised the importance of cost control and accountability mechanisms and suggested that the authorities should have regard to securing best value for money in carrying out resolutions. One respondent argued that the FSCS should only be required to contribute to costs directly related to depositor protection.

2.3 Respondents raised a range of other issues about the FSCS levy arrangements. Some respondents expressed a view that non-deposit-taking financial services companies should not have to contribute to SRR costs through the general retail pool. Other areas of concern included the potential introduction of FSCS pre-funding; changes to the EC Deposit Guarantee Schemes Directive, which could necessitate a review of the policy; and the FSA's ability to alter compensation levels without consultation.

2.4 The Government remains of the view that it would be unworkable to restrict the costs that can be charged to the FSCS to those directly associated with the protection of depositors. The FSCS contribution to SRR costs is capped at the amount that would have been paid had the failed firm had gone into insolvency. Industry will have to pay out no more than it would have had to pay if the Government had not intervened.

2.5 Securing best value for money in resolutions would not be a matter for these regulations. The Banking Act 2009 provides that in carrying out a resolution, the authorities must balance the five statutory special resolution objectives. These objectives cover the key elements of a successful SRR action: protecting financial stability, protecting depositors and protecting property rights. The authorities would be likely to consider costs to industry as part of their wider consideration of how best to balance the special resolution objectives.

2.6 On accountability more generally, the Government remains of the view that it is appropriate that the authorities are accountable through Parliament to the wider public for the way that they have gone about achieving the special resolution objectives. There are measures in place for independent assessment of costs that the FSCS may be expected to bear. As well as provision for the net costs of the resolution to be independently verified, the legislation explicitly requires the appointment of an independent valuer to calculate the amounts the FSCS would recover from the bank under a hypothetical insolvency and ensures that the limit on the maximum amount that the FSCS can be required to contribute is reduced by this amount.

2.7 The operation of the general retail pool and FSCS levy structure more generally are matters for the FSA, not these regulations. The FSA will be undertaking another funding model review during 2010-11, which will invite views on the structure of FSCS funding classes. Whatever the levy structure, the Government's view is that where Government action has averted the need

for a FSCS compensation payout, it is reasonable that those who would otherwise have been liable to contribute can instead be called upon to make an equivalent contribution to the costs of resolution.

Q2. What are your views on whether the "information and assumptions" required to be given to the FSCS should be set out in more detail?

Q3. What additional information is needed to enable the nature, scale and scope of the costs to be understood?

2.8 Some respondents to the consultation proposed that the information and assumptions on which the calculation is based should be set out in more detail, to be challenged or questioned by an appropriate oversight body. It was also suggested that the Treasury should provide information of sufficient detail to enable that FSCS can assure itself (and its levy payers) that the costs are reasonable and that value has been achieved. Some stakeholders requested a clearer definition of 'recoveries', which are subtracted from costs.

2.9 It was emphasised that approximate costs should be conveyed to levy payers as soon as possible, for accounting purposes. One respondent proposed that a formal mechanism should be established for the Treasury to measure the impact of the repayment schedule on levy payers.

2.10 On balance, the Government considers that requirements for information to be supplied in connection with a resolution should not be specified too precisely. It would be difficult to judge in advance precisely the information that would be available in a particular resolution. The authorities are accountable through Parliament to the wider public for the way that they have gone about achieving the special resolution objectives, including for any costs incurred.

Q. 4 What are your views on whether there should be greater clarity about the purpose of the independent verification process?

2.11 Some respondents expressed the view that the independent verification process should cover the cost-effectiveness of spending in a resolution. One respondent expressed the view that the basis of the verification should be published.

2.12 The Government has a range of objectives in carrying out a resolution, not just minimising costs to industry. The Government continues to believe that it is appropriate that the authorities are accountable through Parliament to the wider public for the way that they have gone about achieving the special resolution objectives, including for any costs incurred. However, the draft 2010 Regulations make clear (see regulation 12) that the independent verification should check that expenses attributed to a resolution were incurred in connection with that resolution and that all related recoveries have been taken into account.

Q. 5 What are your views on replacing the High Court or Court of Session with the Financial Services and Markets Tribunal as the forum for review of the independent valuer's decisions?

2.13 There was no consensus among respondents on the question of whether the High Court or Court of Session should be replaced with the Financial Services and Markets Tribunal as the forum for review of the independent valuer's decisions, and respondents requested more information about the rationale for the change.

2.14 The reason for the proposed change is that the Financial Services and Markets Tribunal would be a more suitable specialist tribunal than the High Court or Court of Session to consider technical questions about the valuation and likely timing of recoveries in a hypothetical winding up scenario. The Tribunal is a fully independent body.

2.15 On balance, the Government is of the view that it would still be appropriate to make this change. However, following a reorganisation of tribunals, the Financial Services and Markets Tribunal is to be replaced in April this year by the Upper Tribunal established under the Tribunals, Courts and Enforcement Act 2007. References to the Tribunal in the draft 2010 Regulations are to that Tribunal.

Q.6 What are your views on regulation 11?

2.16 Most stakeholders did not offer views on the appropriateness of regulation 11. One expressed agreement with Government policy that regulation 11 should provide assignment of rights of action against third parties to the FSCS and enable the FSCS to obtain information from failed banks. Regulation 17 of the draft 2010 Regulations restates regulation 11 with some minor improvements.

Q.7 Are there any specific consequences of making contributions to SRR costs which need to be included or excluded by the regulations?

2.17 One respondent commented on the presence in the market of banks backed by the Government. This issue is not directly relevant to these regulations.

3 The draft 2010 Regulations

3.1 This section summarises the main provisions of the draft 2010 Regulations and highlights any significant differences from the 2009 Regulations. Comments are invited on all aspects of the draft 2010 Regulations but there are no specific consultation questions on particular general matters or individual regulations.

3.2 The purpose of the draft 2010 Regulations is to give effect in detailed provisions and practical arrangements to the provisions in sections 214B – 214D FSMA[1] which enable the authorities to recover the costs they incur in a bank resolution (under the special resolution regime (SRR) in Part 1 of the Banking Act 2009) from the FSCS. FSCS contributions to SRR resolution costs are limited to the costs the FSCS would have incurred if the banking institution concerned had gone into default and the FSCS had paid compensation under scheme rules and made recoveries from the winding up of the institution.[2] This limit ("the FSCS cap") has to be determined from an assessment of the compensation costs the FSCS would have paid (which the FSCS itself is responsible for making) and an assessment of the likely recoveries that would have been made from the insolvency firm (which an independent valuer is responsible for making).

3.3 The most important difference between the new provisions and those made under the original section 214B is that the new provisions allow the authorities to recover their cost of funding an SRR resolution (i.e. interest on money borrowed to meet resolution expenses) and increase the FSCS cap to take account of the costs to the FSCS in funding a compensation payout (i.e. interest on the money the FSCS would have borrowed to make compensation payments). For the Treasury to be able to calculate these costs correctly, additional information will be needed from both the FSCS and the valuer:

- the FSCS will have to calculate both the amount and the timing of compensation payments it would have paid out in the event that the bank had gone into insolvency; and
- the valuer will have to calculate both the amounts and timing of the dividends the FSCS would have been paid in the liquidation of the failed bank.

The draft 2010 regulations therefore include detailed provision about this information and the more complex calculations that are required.

3.4 In addition:

- the Treasury may specify principles to the valuer and the FSCS to be taken into account to when making these calculations, to ensure that the valuer and the FSCS make consistent assumptions about timing for example. The Treasury may also specify methods the FSCS should use and any matters that should or should not be taken into account;

[1] Section 214B FSMA was originally inserted by section 171 of the Banking Act 2009. It is to be replaced by sections 214B, 214C and 214D FSMA if clause 28 of the Financial Services Bill is enacted.

[2] A banking institution is a bank, building society or other deposit-taking firm authorised by the FSA.

- there is also revised provision for the situation when the FSCS is required to make a payment towards the costs of resolution before the end of the resolution. This will ensure as far as possible that the FSCS does not make excessive contributions that the Treasury has to then refund at the end of the resolution. The FSCS itself will also be able to make payments before the dates on which they are required, subject to the Treasury's consent;

- certain provisions relating to the treatment of recoveries, actual compensation paid by the FSCS and the independent verification of expenses and recoveries has been clarified; and

- the draft 2010 Regulations provide for the substitution of the Upper Tribunal for the High Court and Court of Session to hear appeals about the determination of the valuer, or to decide other disputes arising under the draft 2010 Regulations in connection with calculations or assumptions made.

3.5 The draft 2010 Regulations also make a number of small improvements and corrections to the 2009 Regulations which are not discussed in this consultation document. There are a number of places where wording which is included in 2009 Regulations has been omitted from the draft 2010 Regulations as the provision is instead made by new sections 214B - 214D FSMA.

Regulation 3 – liability of the scheme

3.6 This regulation sets out the expenses ("eligible expenses") to which the FSCS may be required to contribute. It largely follows regulation 3 of the 2009 Regulations but also makes clear that expenses incurred in connection with the appointment of the valuer, the independent valuer in accordance with section 54, and the person responsible for verifying the accounts kept by and the expenses and recoveries made by the authorities, may be recovered. In the 2009 Regulations, these items were implicitly covered as expenses incurred in connection with the transfer of property, rights and liabilities of the banking institution. There is no explicit reference to the authorities' cost of funding as an expense; this is not needed as new section 214B(4) of FSMA makes clear that interest is an expense for these purposes. The reference in the 2009 Regulations in regulation 3(a) to payments in connection with the transfer of rights and liabilities of the banking institution in respect of protected deposits is also not needed as it is covered by new regulation 3(a).

Regulation 4 – initial notification

3.7 This regulation sets out the information that must be included in the notification given by the Treasury to the FSCS at the start of a resolution if the FSCS is to be required to contribute to SRR resolution costs. The notification is to provide information as to the bank institution involved, the type of stabilisation power exercised and further details of the resolution including the expenses incurred and expected to be incurred. It also includes:

1 requirements to notify the FSCS of the interest rate (which may be fixed or floating) to be used for calculating the authorities' cost of funding a resolution and the cost of funding the FSCS would have had to pay if it had paid compensation to depositors and borrowed to meet that cost, and the periods for which this rate would apply;

2 principles which the FSCS will be required to apply, methods to be used and matter that should or should not be taken into account when the FSCS is making its determinations in accordance with regulation 6; and

3 details as to when the FSCS will be required to make the payment.

Regulation 5 – further notification

3.8 This regulation provides for further notifications to the FSCS if circumstances have changed and the initial notification needs to be updated. These would be made where further expenses have been incurred, recoveries have been made by the authorities, there are changes to the interest rate and the periods for which it is to apply or where the Treasury expect a material change to the level of expenses expected to be incurred or recoveries expected to be made.

Regulation 6 – the scheme manager's expenditure

3.9 This regulation follows regulation 5(2) of the 2009 Regulations to the extent it can given that the required determinations are now set out in full in section 214D(2) FSMA. It also requires the FSCS to keep a record of actual net expenses incurred by the FSCS in the resolution process to deal with cases where the FSCS pays compensation to eligible claimants whose deposits could not be transferred.

Regulation 7 – calculation of the net cost of resolution

3.10 This regulation introduces Schedule 1 and requires the Treasury to keep accounts of the actual cost of the resolution and of the actual recoveries which are made to calculate the net cost of the resolution. The detailed calculations required, including for the addition of interest, are set out in Part 1 of Schedule 1.

Regulation 8 – calculation of the scheme manager's limit

3.11 This regulation requires the Treasury to calculate the FSCS cap using the determinations of the FSCS notified to the Treasury under regulation 6 and those of the valuer notified under regulation 13. The detailed calculations required, including for the addition of interest, are set out in Part 2 of Schedule 1.

Regulation 9 – interim payment

3.12 This regulation sets out the steps that have to be followed before the FSCS can make an interim payment towards the cost of the resolution. It provides for interim payments to be made either on the stipulation of the Treasury or voluntarily by the FSCS with the Treasury's consent.

3.13 Paragraphs (4), (5) and (6) allow the Treasury to request information from the FSCS in order to enable it to estimate the maximum allowable interim payment that the FSCS can make. using the steps in Schedule 1 (paragraph (8)). The maximum allowable interim payment is the maximum amount payable to not automatically require the Treasury to have to refund the FSCS at the end of the process when the final calculations of the net cost of resolution and the scheme manager's limit are known.

3.14 Paragraphs (9) to (12) provide for the FSCS to propose making an interim payment. The maximum allowable interim payment is to be estimated by the Treasury in the same way as for interim payments to be made at the stipulation of the Treasury. Paragraph (13) provides that the FSCS may not make an interim payment without the Treasury's consent.

3.15 Paragraph (14) requires the Treasury to keep an account of all interim payments made in order to calculate the total cost of interim payments. The calculations required, including for the addition of interest, are set out in Part 3 of Schedule 1.

Regulation 10 – final notification (no interim payments)

3.16 This regulation provides for the Treasury to notify the FSCS of the contribution it has to make towards resolution costs at end of a resolution if there have been no interim payments.

The amount of the contribution is simply the lower of the net cost of resolution and the scheme manager's limit.

Regulation 11 – final notification where there have been interim payments

3.17 This regulation provides for the calculation and payment of the final balancing payment by or to the FSCS when interim contributions to the cost of a resolution have already been paid. The method for calculating the balancing payment is set out in Part 4 of Schedule 1 but the principle is that the FSCS has to pay a balancing payment if the final contribution calculated in regulation 10 exceeds the total cost of the interim contributions made.

Regulation 12 – independent verification

3.18 This regulation provides for the independent verification of the accounts kept, actual expenses paid and actual recoveries made by the authorities during a resolution. This clarifies the provision for independent verification made in regulation 5(7) of the 2009 Regulations.

Regulation 13 – appointment and determinations of the valuer

3.19 This regulation largely follows regulations 7 and 8 of the 2009 Regulations save that the Treasury may now specify principles to be applied, methods to be use or matters to be or not to be taken into account by the valuer. It also introduces Schedule 2 (which largely follows the Schedule to the 2009 Regulations).

Regulation 14 – reconsideration of the valuer's determinations

3.20 This regulation confers jurisdiction on the Upper Tribunal to hear appeals of the valuer's reconsidered determinations. It largely follows regulation 9 of the 2009 Regulations but with the substitution of the Upper Tribunal for the High Court and Court of Session.

Regulation 15 – reference to the Tribunal

3.21 This regulation confers jurisdiction on the Upper Tribunal to resolve disputes arising under the regulations in respect of calculations or assumptions made, or issues relating to the making of payments. It largely follows regulation 10 of the 2009 Regulations but with the substitution of the Upper Tribunal for the High Court and Court of Session.

Regulation 16 – proceedings before the Tribunal

3.22 This regulation introduces Schedule 3 which makes provision for proceedings before the Upper Tribunal arising from references under regulation 14(5) or regulation 15.

Regulation 17 – payments made under these Regulations to constitute payment of compensation under the scheme

3.23 This regulation largely follows regulation 11 of the 2009 Regulations. It ensures that a depositor, having had their deposit transferred to a new banking institution, will be unable to claim for compensation for the value of that deposit from the FSCS.

Regulation 18 – transitional provision for previous notifications

3.24 This regulation makes transitional provision to ensure that any notifications made under the 2009 Regulations (e.g. those made in respect of the Dunfermline Building Society) can be treated as notifications under the draft 2010 Regulations with necessary modifications. In particular, provision is made for the addition of interest from 19 November 2009 – which was the date of the Economic Secretary's announcement that interest would be added to resolution

costs and the FSCS cap and of the introduction of the Financial Services Bill in the House of Commons.[3]

Schedule 1

3.25 This schedule sets out the detailed methods for calculating the net cost of resolution of resolution (Part 1), the scheme manager's limit (Part 2), the total cost of interim payments (Part 3) and the balancing payments (Part 4).

Schedule 2

3.26 This schedule largely follows the schedule to the 2009 Regulations. It makes detailed provision for the remuneration and removal of the valuer (Part 1) and for applications to the court by the valuer to require a person to provide information for the purpose of assessing recoveries and the timing of such recoveries (Part 2).

Schedule 3

3.27 This schedule makes detailed provision for proceedings before the Upper Tribunal (Part 1) and for offences in connection with those proceedings concerning the valuer's determination under section 214D(3) (Part 2).

[3] The Economic Secretary's written ministerial statement can be found in Hansard for 19 November 2009 in columns 1WS – 3WS, available on the UK Parliament website (www.parliament.uk).

4 How to respond

4.1 This consultation will last until 15 June 2010. Please ensure that your response reaches us by the closing date. Please send responses to:

Financial Regulation Strategy team
International & Finance Directorate
HM Treasury
1 Horse Guards Road
London
SW1 2HQ

Email: banking.reform@hmtreasury.gsi.gov.uk

4.2 When responding please state if you are responding as an individual or representing the views of an organisation. In accordance with the code of practice on open government comments will be made publicly available unless respondents specifically request otherwise.

4.3 An impact assessment for these policy measures are included in the impact assessment for the Financial Services Bill, which was introduced into Parliament on 19 November 2009. More information about the Financial Services Bill is available from the Treasury website (www.hm-treasury.gov.uk). A copy of this impact assessment is also included below.

Confidentiality disclosures

4.4 Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act (DPA) and the Environmental Information Regulations 2004. If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply with and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality will be maintained in all circumstances.

4.5 An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department. Your personal data will be processed in accordance with the DPA, and in the majority of circumstances, this will mean that your personal data will not be disclosed to third parties.

Freedom of Information contact

4.6 Any Freedom of Information Act queries should be directed to:

Correspondence and Enquiry Unit
Freedom of Information Section
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
Tel: (+44) (0) 20 7270 4558
Fax: (+44) (0) 20 7270 4681

Email: public.enquiries@hm-treasury.gov.uk

Code of practice on consultation

4.7 This consultation is being conducted in line with the criteria in the Government's Code of Practice on Consultation.[1] The seven consultation criteria are:

- When to consult – formal consultation should take place at a stage when there is scope to influence the policy outcome.
- Duration of consultation exercises – consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
- Clarity of scope and impact – consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
- Accessibility of consultation exercises – consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
- The burden of consultation – keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
- Responsiveness of consultation exercises – consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
- Capacity to consult – officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

4.8 If you feel this consultation does not fulfil these criteria, please contact:

Angela Carden
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Email: angela.carden@hmtreasury.gsi.gov.uk

[1] Available on the Department for Business, Innovation and Skills at http://www.berr.gov.uk/whatwedo/bre/consultation-guidance/page44458.html.

A Impact assessment

A.1 This impact assessment is reproduced from the impact assessment for the Financial Services Bill,[1] which was introduced into the House of Commons on 19 November 2009.

[1] See *Financial Services Bill: Impact Assessment* (www.hm-treasury.gov.uk/d/fin_bill_ias.pdf)

Summary: Intervention & Options

Department /Agency:	Title:	
HM Treasury	**Impact Assessment of allowing the cost of funding the exercise of SRR powers to be recovered from the FSCS**	
Stage: final proposal	**Version:** 1	**Date:** 1 November 2009
Related Publications: Banking Bill Impact assessment (October 2008) paragraphs 1.173 - 1.182		

Available to view or download at:
http://www.hm-treasury.gov.uk

Contact for enquiries: David Sly **Telephone:** 020 7270 5162

What is the problem under consideration? Why is government intervention necessary?

The costs of SRR powers can be recovered from the FSCS up to the net costs the FSCS would have incurred had the bank gone into default and FSCS compensation paid in the normal way. Both the actual SRR costs and the counterfactual FSCS costs would be spread over time and involve both inflows and outflows. But no allowance can currently be made for the interest costs or receipts that would arise because of these timing differences. So the true economic cost of an SRR cannot be recovered from the FSCS up to a cap based on the true economic cost to the FSCS in the counterfactual.

What are the policy objectives and the intended effects?

The policy objective (and intended effect) is to ensure that the true economic cost of the use of SRR powers can be recovered from the FSCS subject to a cap that would be consistently calculated from the true economic costs that the FSCS would have had to meet in the counterfactual.

What policy options have been considered? Please justify any preferred option.

There are only two options - "do nothing" and the preferred option. The preferred option will ensure that true economic costs of the SRR can be recovered from the FSCS up to a limit that reflects as accurately as possible the true economic costs that the FSCS would have incurred in the counterfactual - the scenario in which the bank defaulted and the FSCS paid compensation and made recoveries from the estate in the normal way.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The policy will be reviewed as part of any review of the special resolution regime and Parts 1 - 3 of the Banking Act 2009.

Ministerial Sign-off For final proposal/implementation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

..... Date: 19 November 2009

Summary: Analysis & Evidence

Policy Option:	Description:

COSTS

ANNUAL COSTS	Description and scale of **key monetised costs** by 'main affected groups'
One-off (Transition) **Yrs**	
£	
Average Annual Cost (excluding one-off)	
£	**Total Cost** (PV) **£**

Other **key non-monetised costs** by 'main affected groups' Cost of funding SRR costs transferred from the Exchequer to FSCS levy payers. This is a transfer and aggregate cost on both groups is zero. There will be a small additional resource cost arising from extra activity by an independent valuer; this cost will fall on the Exchequer.

BENEFITS

ANNUAL BENEFITS	Description and scale of **key monetised benefits** by 'main affected groups'
One-off **Yrs**	
£	
Average Annual Benefit	
£	**Total Benefit** (PV) **£**

Other **key non-monetised benefits** by 'main affected groups'

Key Assumptions/Sensitivities/Risks

Price Base Year	Time Period Years	**Net Benefit Range** (NPV) **£**	**NET BENEFIT** (NPV Best estimate) **£**

What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	2009
Which organisation(s) will enforce the policy?	N/A
What is the total annual cost of enforcement for these	£
Does enforcement comply with Hampton principles?	N/A
Will implementation go beyond minimum EU requirements?	N/A
What is the value of the proposed offsetting measure per year?	£
What is the value of changes in greenhouse gas emissions?	£ Nil
Will the proposal have a significant impact on competition?	No

Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase £ Decrease £ **Net** £

Key: **Annual costs and benefits: Constant Prices** **(Net) Present Value**

Evidence Base

The Banking Act 2009 introduced a special resolution regime (SRR) to provide for the more efficient resolution of failing banks and building societies. The SRR was used for the first time to resolve the Dunfermline Building Society at the end of March 2009. This measure will be applied from 19 November 2009 (the date of introduction of the Financial Services Bill) so as to ensure that the Exchequer can recover the opportunity cost of the funds it has contributed towards the cost of resolving the Dunfermline Building Society from the Financial Services Compensation Scheme (FSCS).

The SRR includes powers under which the Authorities can arrange for the transfer of the assets and liabilities of a failing institution, as well as shares and other securities issued by that institution to commercial purchasers, to a "bridge bank" owned by the Bank of England or into temporary public ownership. The SRR also allows for the payment of compensation to transferors and to third parties. Costs will also be incurred to make up the value of assets transferred to a person to whom any liabilities (e.g. customer deposits) have been transferred.

These costs would fall on the Authorities (to the extent they cannot be met from the assets of the failed bank). However, the Banking Act 2009 also amended the Financial Services and Markets Act 2000 (FSMA) to provide for the FSCS to contribute to the costs of the use of SRR powers. This is appropriate because, if the SRR was not used, the institution would have defaulted and the FSCS would have had to pay compensation to depositors in the institution in accordance with the rules. In those circumstances, the FSCS would also have taken over the depositors' claims on the failed institution and made recoveries from the assets of the failed institution on its winding up. It is also appropriate, therefore, that the maximum amount the FSCS can be required to contribute is capped at the net cost that it would have incurred in this counterfactual scenario. The cap is set at the compensation the FSCS would otherwise have paid less the amount of the recoveries that it would have made from the winding up.

Unfortunately, the theoretical scheme just described (and which was implemented in FSMA and the FSMA (Contribution to Costs of Special Resolution Regime) Regulations 2009) did not take account of the time that both a bank resolution would take or that the winding up of a bank would take in the counterfactual scenario. In both scenarios, the Authorities and the FSCS would have to finance payments of compensation or resolution costs until these were reduced or eliminated by actual or hypothetical recoveries from the disposal of the assets of the failed bank and costs of financing would be incurred. These costs would be explicit if either the FSCS or the Treasury borrowed money specifically to finance the payments they made but there would always be an opportunity cost since, however the money paid was raised, the funds could always have been diverted to an alternative use. But FSMA does not allow the Treasury to recover the opportunity cost of funds used from the FSCS and it does not allow the cost of the funds that the FSCS would hypothetically have to raise in the counterfactual to be taken into account in setting the cap on the contribution the FSCS can be required to make to SRR costs.

The overall effect of this omission is that the contribution the FSCS can make to SRR costs is likely to be less than the net costs it would actually have incurred in paying compensation when an institution failed. However, the proportional extent of the shortfall would depend on the timing of recoveries and on differences in the patterns of recoveries in the SRR and in the counterfactual scenario. The amount of any shortfall would also depend on the size of the failing institution. However, based on estimates made in connection with some recent resolutions, the shortfall could range from between £½ billion to £3 billion. It is not possible to quantify this more precisely for the reasons just given.

The shortfall would means the cost to the Exchequer of resolving failing institutions is higher than it otherwise would be. If the proposed reforms are enacted, this cost will be borne in the first instance by the FSCS and will be met ultimately by increased levies on the financial services

industry. The proposal therefore implies a transfer from the FSCS levy payers to the Exchequer. But this is not a resource cost and accordingly there is no difference in resource costs between the "do nothing" and the preferred options.

However, there will be higher resource costs in the "preferred" option to the extent that more work is involved in estimating the limit on the FSCS contribution to SRR costs in the counterfactual scenario. Under the system introduced in the Banking Act, an independent valuer has to be appointed to estimate the amount of recoveries (dividends from the winding up) the FSCS would have made in the counterfactual scenario. In the preferred option, the valuer is likely to have to consider in more detail when the FSCS would have made recoveries so that the cost of funding can be calculated more accurately. (Recoveries are a financial inflow so they will reduce the amount of compensation or payments that has to be funded and hence, of course, the cost of that funding.) The preferred option seems likely, therefore, to require more work by the independent valuer and this implies some additional resource costs. It is not possible to quantify these additional costs but it seems unlikely that they would be significant in comparison with the amounts of the shortfall discussed above, or as an addition to the costs already incurred in appointing a valuer.

The extra costs on FSCS levy payers will be divided among the levy payers in accordance with the appropriate FSCS rules (which are made by the FSA). In general, the effect of these rules is that levies are divided between institutions in proportion to the size of their deposit base. These additional costs will not fall disproportionately on small firms and are unlikely to affect competition between financial services firms. No other specific impact test is relevant.

B Draft Statutory Instrument

Draft Regulations laid before Parliament under sections 429(2) of the Financial Services and Markets Act 2000, for approval by resolution of each House of Parliament.

DRAFT STATUTORY INSTRUMENTS

2010 No.

FINANCIAL SERVICES AND MARKETS

The Financial Services and Markets Act 2000 (Contribution to Costs of Special Resolution Regime) Regulations 2010

Made - - - - ***

Coming into force in accordance with regulation 1(1)

The Treasury, in exercise of the powers conferred by sections 214B, 214D and 428(3) of the Financial Services and Markets Act 2000(**a**) make the following Regulations:

Citation, commencement and revocation

1.—(1) These Regulations may be cited as the Financial Services and Markets Act 2000 (Contribution to Costs of Special Resolution Regime) Regulations 2010 and shall come into force on the day after the day on which they are made.

(2) The Financial Services and Markets Act 2000 (Contribution to Costs of Special Resolution Regime) Regulations 2009(**b**) ("the former Regulations") are revoked.

Interpretation

2.—(1) In these Regulations—

"the Act" means the Financial Services and Markets Act 2000;

"the 2009 Act" means the Banking Act 2009;

"actual account" has the meaning set out in paragraph 7 of Schedule 1;

"banking institution" means—

(a) a bank (within the meaning of section 2 of the 2009 Act),

(b) a building society (within the meaning of section 119 of the Building Societies Act 1986(**c**)),

(c) a holding company (within the meaning of section 82 of the 2009 Act), or

(d) if an order has been made under section 89 of the 2009 Act applying Part 1 of that Act to credit unions (within the meaning of section 31 of the Credit Unions Act 1979(**d**) or, in

(**a**) 2000 c.8. Section 214B was substituted and sections 214C and 214D were inserted by section 28 of the Financial Services Act 2010 c.[ ].
(**b**) S.I. 2009/807.
(**c**) 1986 c.53.
(**d**) 1979 c.34.

Northern Ireland, Article 2 of the Credit Unions (Northern Ireland) Order 1985(**a**)), a credit union;

"COMP Sourcebook" means the Authority's Compensation Sourcebook as amended from time to time, made by the Authority under the Act;

"court" means the High Court or the Court of Session;

"determination notice" has the meaning set out in regulation 13(5);

"eligible claimant" means a person who is eligible to make a claim under the scheme in respect of a deposit at a banking institution (see rule 4.2.1. of the COMP Sourcebook);

"eligible expenses" has the meaning set out in regulation 3;

"expenses account" has the meaning set out in paragraph 1 of Schedule 1;

"FEES 6 Chapter" means Chapter 6 (Financial Services Compensation Scheme Funding) of the Fees Manual as amended from time to time, made by the Authority under the Act;

"final notification" has the meaning set out in regulation 10 where the scheme manager has not made an interim payment, and in regulation 11 where it has;

"further notification" has the meaning set out in regulation 5(1);

"in default" means in default in accordance with rule 6.3.1 of the COMP Sourcebook;

"information notice" has the meaning set out in regulation 9(4);

"initial notification" has the meaning set out in regulation 4(1);

"interim payment" has the meaning set out in regulation 9(1);

"net cost of resolution" has the meaning set out in paragraph 6 of Schedule 1;

"notified rate" has the meaning set out in regulation 4(2)(f);

"notional account" has the meaning set out in paragraph 7 of Schedule 1;

"other person" has the meaning set out in regulation 4(2)(d);

"protected deposit" means a protected deposit under the scheme (see rule 5.3.1 of the COMP Sourcebook);

"qualifying claimant" means an eligible claimant who, if the banking institution were to have been in default immediately before the relevant time, would have had a claim against the banking institution, or in the case of a banking institution which is a holding company would have had a claim against one more of its subsidiary companies, in respect of a protected deposit;

"reconsidered determination notice" has the meaning set out in regulation 14(3);

"recoveries account" has the meaning set out in paragraph 1 of Schedule 1;

"relevant time" means the time at which a stabilisation power takes effect in respect of a banking institution and, if more than one stabilisation power is exercised, means the time at which the first stabilisation power so exercised takes effect;

"resolution" means the exercise of a stabilisation power;

"scheme" means the compensation scheme;

"scheme manager's limit" has the meaning set out in regulation 8(1);

"stabilisation power" means one of the stabilisation powers referred to in section 1(4) of the 2009 Act and a reference to the exercise of a stabilisation power includes the exercise of more than one stabilisation power in respect of or in connection with the same banking institution;

"in temporary public ownership" means that a share transfer order has been made under, or in accordance with, section 13(2) of the 2009 Act and the banking institution is wholly owned by a nominee of the Treasury or a company wholly owned by the Treasury;

"total cost of interim payments" has the meaning set out in paragraph 19 of Schedule 1;

(**a**) S.I. 1985/1205 (NI 12).

"voluntary interim payment" has the meaning set out in regulation 9(2); and

"voluntary payment notice" has the meaning given in regulation 9(9).

(2) Any reference in these Regulations to sections 214B, 214C or 214D are to those sections of the Act.

(3) A notification given under these Regulations by the Treasury or the scheme manager may be given in writing by such means as the notifier considers appropriate.

Liability of the scheme

3. The descriptions of expenses in respect of which the Treasury may require the scheme manager to make payments under section 214B(2) ("eligible expenses") are—

(a) expenses incurred in connection with the transfer of property, rights or liabilities of the banking institution under a stabilisation power;

(b) payments made to a bank administrator in connection with the pursuit of Objective 1 in respect of the banking institution (and "bank administrator" and "Objective 1" have the meanings given in sections 141 and 138 of the 2009 Act respectively);

(c) expenses incurred in connection with taking the banking institution into temporary public ownership in accordance with sections 13 or 82 of the 2009 Act; and

(d) expenses incurred in connection with the appointment of —

(i) an independent valuer in accordance with an order made under section 54 of the 2009 Act,

(ii) a valuer under section 214D(3), or

(iii) a person to perform the verification under regulation 12.

Initial notification

4.—(1) Where the Treasury requires the scheme manager to make payments under section 214B(2), the Treasury shall send the scheme manager a notification as soon as reasonably practicable ("the initial notification").

(2) The initial notification shall include—

(a) the name and address of the banking institution in respect or in connection with which a stabilisation power has been exercised;

(b) a statement that the Treasury think that the banking institution was, or was likely to have been, or but for the exercise of the stabilisation power, would have become, unable to satisfy claims against it;

(c) details of the stabilisation power exercised, when it was exercised and the identity of the transferee (if any);

(d) the eligible expenses incurred, or an estimate of those expected to be incurred, by the Treasury or any other person other than the scheme manager ("the other person") and an estimate of any recoveries the Treasury or the other person expects to make in respect of the banking institution;

(e) if—

(i) a payment is required immediately from the scheme manager, a demand for that payment setting out the amount as calculated in accordance with regulation 9, and when and to whom the payment is due, or

(ii) if a payment is not required immediately from the scheme manager, an estimate as to when the scheme manager is likely to be required to make a payment or a date before which the payment will not be required;

(f) the interest rate ("the notified rate") which will apply to the amounts required to be paid under regulations 10(4), 11(3) or (4), and the accounts kept in accordance with Schedule 1 and information as to—

(i) the basis for how the notified rate is to be calculated: whether this is to be a fixed rate, or a floating rate dependent on an underlying rate (and, if so, information as to this underlying rate), and

(ii) the period or successive periods for which the notified rate shall apply;

(g) any specified principles, methods or matters which, in accordance with sections 214D(4) or (5), the scheme manager will be required to apply, use or take into account when making its determinations under section 214D(2); and

(h) any further information that the Treasury consider necessary in respect of the payments to be made.

(3) No change can be made to the notified rate under paragraph (2)(f), or to the basis on which it is calculated, before the end of the period or periods notified.

(4) A failure to include any of the information in paragraph (2) in the initial notification does not render that notification invalid.

Further notification

5.—(1) Where an initial notification has been sent to the scheme manager, the Treasury must send a further notification ("further notification") to the scheme manager as soon as reasonably practicable if at any time before the Treasury issue a final notification—

(a) further expenses have been incurred by the Treasury or the other person in connection with the exercise of the stabilisation power;

(b) recoveries have been made by the Treasury or the other person in respect of the banking institution;

(c) there is a change in the notified rate or basis for calculating the notified rate, or the period or periods for which the notified rate is to apply; or

(d) the Treasury expect a material change to the level of expenses expected to be incurred or recoveries expected to be made from that previously notified;

updating the information contained in the initial notification where relevant.

(2) A further notification must also be sent to the scheme manager where at any time after the initial notification the Treasury require the scheme manager to make an interim payment, and the requirement for the interim payment was not included in the initial notification.

(3) A further notification under paragraph (2) shall set out the amount of the payment required (as calculated in accordance with regulation 9), and when and to whom it is due.

The scheme manager's expenditure

6.—(1) Following receipt of the initial notification under regulation 4, the scheme manager shall —

(a) make the determinations required by section 214D(2); and

(b) keep a record of the actual expenditure it incurs in respect of the banking institution, including —

(i) when it incurs the expenditure, and

(ii) details of any recoveries made by the scheme manager in respect of the actual expenditure (including when such recoveries are made).

(2) In making the determinations under section 214D(2) the scheme manager will use any methodology or approach it considers appropriate, (subject to any requirements specified in the initial notification in accordance with regulation 4(2)(g)) when making the determinations.

(3) Once the scheme manager has made the determinations under section 214D(2), and is satisfied that, to the best of its knowledge, it will not incur any further actual expenses nor make any further recoveries, the scheme manager will notify the determinations to the Treasury together with the record of the actual expenditure.

Calculation of the net cost of resolution

7. Following the sending of the initial notification to the scheme manager, the Treasury shall keep the accounts specified in Part 1 of Schedule 1.

Calculation of the scheme manager's limit

8.—(1) On receipt of—

(a) the determinations of the scheme manager and the record of actual expenditure under regulation 6(3);

(b) the determinations or reconsidered determinations of the valuer under regulations 13 and 14; and

(c) an acknowledgement from the scheme manager that it does not intend to—

(i) require the valuer to reconsider the determinations under regulation 14(1),

(ii) refer the valuer's reconsidered determination to the Tribunal under regulation 14(5), or

(iii) make a reference to the Tribunal under regulation 15(1) or appeal any determination of the Tribunal;

the Treasury shall determine the limit of the amount of special resolution regime payments that can be required to be made under section 214B(2) in accordance with section 214C(1) ("the scheme manager's limit") using the methodology set out in Part 2 of Schedule 1.

(2) The Treasury may assume that the scheme manager does not have the intention referred to in paragraph (1)(c) if the Treasury have asked the scheme manager for an acknowledgement, 14 days have passed and the scheme manager has not indicated anything to the contrary.

Interim payment

9.—(1) This regulation applies where the Treasury require the scheme manager to make an interim payment ("interim payment") in respect of the banking institution before the Treasury have sent out a final notification.

(2) This regulation also applies where the scheme manager proposes to make an interim payment voluntarily ("voluntary interim payment").

(3) The total amount of interim payments made by the scheme manager must not be such as to give rise to an expectation that an amount will be required to be repaid to the scheme manager (once the accounts kept in accordance with Schedule 1 have been verified in accordance with regulation 12, and the Treasury has received the valuer's determination under section 214D(3)(a)).

(4) Before sending a notification under regulation 4 or 5 requiring an interim payment from the scheme manager, the Treasury must send the scheme manager an information notice ("information notice").

(5) An information notice may be sent to the scheme manager before the resolution takes place.

(6) The information notice shall require the scheme manager to provide, to the best of its knowledge in the time available, estimates —

(a) of the determinations it will make under section 214D(2); and

(b) of the actual expenditure it expects to incur in respect of the banking institution, including when this is likely to be incurred, and the amount (and timing) of any recoveries in respect of those expenses,

and shall set out the time by which the scheme manager must respond to the notice.

(7) On receipt of the information notice, the scheme manager may request any necessary information from the Treasury and the Treasury shall respond to such a request promptly and to the best of their ability.

(8) On receipt of the information —

(a) using the notified rate (or the intended notified rate as the case may be); and

(b) estimating—

(i) the amount that would have been likely, at the time when the stabilisation power was exercised to be recovered by the scheme manager, and

(ii) the time or times at which the amount would have been likely to have been recovered;

the Treasury shall establish, to the best extent possible using the methods set out in Schedule 1, the maximum amount of interim payments that may be made by the scheme manager. The amount required in the notification under regulations 4 or 5 shall be subject to this maximum amount.

(9) Where the scheme manager proposes to make a voluntary interim payment it must send the Treasury a notice ("voluntary payment notice") at least 14 days before the date on which it proposes to make the payment which contains—

(a) the date on which the scheme manager proposes to make the payment;

(b) the amount it proposes to pay; and

(c) the estimates required under paragraph (6)(a) and (b).

(10) Before sending a voluntary payment notice, the scheme manager may request from the Treasury any information it considers necessary for the making of the estimates specified in paragraph (6)(a) and (b).

(11) On receipt of a voluntary payment notice, using the procedure set out in paragraph (8), the Treasury shall establish the maximum amount of payments that the scheme manager may make under this regulation.

(12) On establishing the maximum amount in paragraph (11), the Treasury shall then determine whether –

(a) to consent to the voluntary interim payment;

(b) to consent to a voluntary interim payment of a different amount (which shall not be greater than the voluntary payment proposed by the scheme manager or the maximum amount established under paragraph (11)); or

(c) not to consent to the voluntary interim payment,

and shall notify their determination to the scheme manager in writing.

(13) The scheme manager shall not make a voluntary interim payment without the Treasury's consent.

(14) Where any interim payment is made, the Treasury shall keep the account specified in Part 3 of Schedule 1 to these Regulations.

Final notification (no interim payments)

10.—(1) This regulation applies where the scheme manager does not make any interim payments.

(2) As soon as reasonably practicable after—

(a) establishing—

(i) the net cost of resolution in accordance with regulation 7, and

(ii) the scheme manager's limit in accordance with regulation 8, and

(b) the undertaking of verification in accordance with regulation 12,

the Treasury shall send a final notification to the scheme manager setting out the amount of the payment due from the scheme manager and to whom that payment should be made.

(3) The amount required from the scheme manager will be the lower of the net cost of resolution and the scheme manager's limit.

(4) Following receipt of the final notification, the scheme manager will pay the amount due, together with interest accruing on that amount at the notified rate from the date the final notification is sent until the date of payment.

Final notification (interim payments)

11.—(1) This regulation applies where the scheme manager has made an interim payment.

(2) After—

(a) the Treasury have established—

(i) the net cost of resolution in accordance with regulation 7,

(ii) the scheme manager's limit in accordance with regulation 8, and

(iii) the total cost of interim payments in accordance with regulation 9, and

(b) verification in accordance with regulation 12;

the Treasury shall calculate the amount of any balancing payment due from the scheme manager or the Treasury in accordance with Part 4 of Schedule 1 and send a final notification to the scheme manager.

(3) Where under the final notification a balancing payment is due from the scheme manager, the final notification shall set out to whom that payment should be made and it shall be paid, together with interest accruing on that amount at the notified rate from the date the final notification is sent until the date of payment.

(4) Where under the final notification a balancing payment is due from the Treasury to the scheme manager, it shall be paid within 7 days together with interest accruing on that amount at the notified rate from the day the final notification is sent until the day of payment.

Independent verification

12. Before sending a final notification under regulation 10 or 11, the Treasury shall appoint an independent person to verify—

(a) the accounts kept in accordance with Schedule 1; and

(b) whether—

(i) the expenses included in the expenses account are eligible expenses, and

(ii) all recoveries made to date by the Treasury or the other person in respect of the banking institution have been included in the recoveries account.

Appointment and determinations of the valuer

13.—(1) Where the person appointed as valuer to make the determinations under section 214D(3) is not the same person as appointed in accordance with an order made under section 54 of the 2009 Act, Part 1 of Schedule 2 shall apply.

(2) The Treasury may specify any principles, methods or matters in accordance with sections 214D(4) or (5) to be applied, used or taken into account by the valuer when making the determinations under section 214D(3).

(3) The valuer may—

(a) do anything necessary or desirable for the purposes of or in connection with making the determinations, and

(b) apply to the court for an order requiring the provision of information reasonably required for making the determinations in paragraph (1) (and, in that event, paragraph 11 of Schedule 2 shall apply.)

(4) Part 2 of Schedule 2 applies to information obtained by the valuer in connection with making the determinations.

(5) When the valuer has made the determinations, the valuer shall give the scheme manager and the Treasury notice in writing ("the determination notice").

(6) The determination notice must contain the following information—

(a) the date on which it is issued;

(b) the determinations made by the valuer under section 214D(3); and

(c) the assumptions and calculations relevant to those determinations.

(7) The scheme manager may publish the determination notice on the scheme's website or in such other way as the scheme manager thinks fit.

Reconsideration of the valuer's determinations

14.—(1) If the scheme manager is or the Treasury are dissatisfied with the determination notice, either may require the valuer to reconsider the determinations.

(2) The request must be made within 3 months of the date of the determination notice, set out the reasons for disputing either or both the determinations and be in writing.

(3) Where the valuer is required to reconsider a determination, the valuer must give the Treasury and the scheme manger notice in writing of their reconsidered determination ("the reconsidered determination notice").

(4) The reconsidered determination notice must contain the information specified in regulation 13(6).

(5) If the scheme manager is or the Treasury are dissatisfied with a reconsidered determination, either may refer it to the Tribunal(**a**).

(6) If the Tribunal requires the valuer to redetermine a reconsidered determination, paragraphs (3), (4) and (7) will apply to any re-determination.

(7) The scheme manager may publish the reconsidered determination notice on the scheme's website or in such other way as the scheme manager thinks fit.

Reference to the Tribunal

15.—(1) A reference may be made to the Tribunal by the Treasury or the scheme manager in order to resolve disputes arising under these Regulations.

(2) A reference may be made in respect of—

(a) a determination made by the scheme manager under section 214D(2);

(b) a calculation made by the Treasury in connection with their functions under these Regulations; or

(c) a dispute relating to the making of payments under these Regulations;

but no reference may be made under this regulation in respect of any determination or reconsidered determination made by the valuer under section 214D(3) or regulation 14.

Proceedings before the Tribunal

16. Where a reference is made under regulation 14(5) or 15, Schedule 3 shall apply.

Payments made under these Regulations to constitute payment of compensation under the scheme

17.—(1) For the purposes of Part 15 of the Act, the COMP Sourcebook and the FEES 6 Chapter, where the stabilisation power exercised in respect of the banking institution has resulted in a qualifying claimant having all or part of their protected deposits held by that institution (or, where

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(**a**) "The Tribunal" means the Upper Tribunal: see section 417(1) of the Act as amended by S.I. 2010/22.

the banking institution is a holding company, held by a subsidiary of that company) being transferred to a new entity—

(a) any payments made by the scheme manager, under these Regulations, in respect of that banking institution, shall constitute payment of compensation to that claimant in respect of claims under the scheme against the banking institution (or as the case may be, the subsidiary) for the amount of their protected deposit transferred;

(b) on the scheme manager receiving the initial notification from the Treasury under regulation 4(1) in respect of the banking institution—

(i) the banking institution, (or if the banking institution is a holding company, the subsidiary of that company holding protected deposits) shall be deemed to be in default for purposes of the COMP Sourcebook and the FEES 6 Chapter,

(ii) each qualifying claimant shall be deemed to have made an application for compensation for the purpose of the COMP Sourcebook and the FEES 6 Chapter in respect of the amount of their protected deposit transferred,

(iii) each qualifying claimant shall be deemed to have accepted an offer of compensation made by the scheme and to have received payment for such compensation for that amount for the purposes of the COMP Sourcebook and the FEES 6 Chapter;

and, accordingly, a qualifying claimant has no right to claim, and the scheme has no obligation to pay, any further compensation in respect of that amount.

(2) For the purposes of this regulation—

(a) where all or part of the business of a banking institution has been transferred to a bridge bank under section 12 of the 2009 Act, although a new entity for the purposes of paragraph (1), the bridge bank is to be treated as being the same banking institution as the institution in respect of which the stabilisation power was exercised;

(b) where a banking institution is in temporary public ownership—

(i) although the same banking institution, it shall be treated as a new entity for the purposes of paragraph (1), but

(ii) when it ceases to be in temporary public ownership it shall be treated as a different banking institution; and

(c) "protected deposit" means all or part of a protected deposit held with the banking institution.

Transitional provision for previous notifications

18.—(1) This regulation applies where, before the coming into force of these Regulations, a notification has been made by the Treasury under regulation 4 of the former Regulations.

(2) A notification (or where revised notifications have been sent, the most recent revised notification) under the former Regulations shall be treated as the initial notification in respect of the banking institution in accordance with regulation 4 of these Regulations.

(3) The scheme manager's assessment of Amount B under regulation 5(2) of the former Regulations shall be treated as its determination under section 214D(2)(a).

(4) As soon as practicable after the coming into force of these Regulations, the Treasury will send an updating notification to the scheme manager setting out—

(a) the total eligible expenses incurred to date in respect of the banking institution;

(b) recoveries made to date by the Treasury or the other person in respect of the banking institution;

(c) if—

(i) the payment is required immediately from the scheme manager, a demand for that payment setting out the amount as calculated in accordance with regulation 9, and when and to whom this payment is due, or

(ii) if the payment is not required immediately from the scheme manager, an estimate as to when the scheme manager is likely to be required to make a payment;

(d) the notified rate; and

(e) any specified principles, methods or matters accordance with sections 214D(4) or (5) that the scheme manager must apply, use or take into account when making the determination under section 214D(2)(b).

(5) Where the Treasury requires the scheme manager to make an interim payment immediately after the coming into force of these Regulations, in regulation 9(4) the reference to "a notification under regulations 4 or 5" means the notification in accordance with paragraph (4).

(6) If a valuer has been appointed to perform the function in regulation 8(1) of the former Regulations, on the coming into force of these Regulations—

(a) the valuer shall be treated as if they were appointed to exercise functions under section 214D(3);

(b) the Treasury shall promptly specify to the valuer any principles, methods or matters to be applied, used or taken into account by the valuer in accordance with section 214D(4) and (5) when making the determination under section 214D(3)(b), and, if no determination notice has been received under regulation 8(6) of the former Regulations, the determination under section 214D(3)(a);

(c) where the Treasury have received the determination notice under regulation 8(6) of the former Regulations, this shall be treated as the valuer's determination under section 214D(3)(a); and

(d) where the valuer has been required to reconsider that determination notice under regulation 9(1) of the former Regulations, if the Treasury have received the revised determination notice, it shall be treated as a reconsidered determination in respect of the valuer's determination under section 214D(3)(a) under regulation 14 above.

(7) Where this regulation applies, Schedule 1 to these Regulations applies with the following modifications—

(a) for paragraph 4, substitute—

"**4.** From 19th November 2009(**a**) (or from the time specified in paragraph 2 if later), interest at the notified rate shall accrue daily on the amount in each account and shall be added to the account on each anniversary of the relevant time, but where the final notification is made on a date falling after an anniversary date, then all accrued interest not yet added, shall be added to the account on the date of the final notification.";

(b) for paragraph 11, substitute—

"**11.** In the notional account the Treasury shall account for interest at the notified rate on the outstanding balance as if it had, as from 19th November 2009 (or from the time specified in paragraph 8 if later), accrued daily and had been added to the account on each anniversary of the relevant time.";

(c) for paragraph 12, substitute—

"**12.** In the actual account the Treasury shall account for interest at the notified rate on the outstanding balance as if it had, as from the 19th November 2009, (or from the time specified in paragraph 8 if later), accrued daily on the outstanding balance and had been added to the outstanding balance on each anniversary of the relevant time."; and

(d) for paragraph 18, substitute—

"**18.** From 19th November 2009 (or from the time specified in paragraph 16 if later), interest at the notified rate shall accrue daily on the amount in the account and shall be added to the account on each anniversary of the relevant time, but where the final

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(**a**) See section 28(2) of the Financial Services Act 2010 (c.[ ])

notification is made on a date falling after an anniversary date, then all accrued interest not yet added shall be added to the account on the date of the final notification.".

Name
Name
[ ] 2010 Two of the Lords Commissioners of Her Majesty's Treasury

SCHEDULE 1

Regulations 7, 8, 9, 11 and 12.

PART 1

Calculation of the net cost of the resolution

1. The Treasury shall keep accounts of eligible expenses incurred ("the expenses account") and of recoveries made ("the recoveries account") by itself or by the other person in respect of the banking institution.

2. The accounts shall be dated from the time when the Treasury or the other person first incurred eligible expenses or made recoveries, whichever is the sooner.

3. The Treasury shall add eligible expenses and recoveries to the appropriate accounts on the dates on which they are incurred or made.

4. Interest at the notified rate shall accrue daily on the amount in each account and shall be added to the account on each anniversary of the relevant time, but where the final notification is made on a date falling after an anniversary date, then all accrued interest not yet added shall be added to the account on the date of the final notification.

5. When the Treasury is satisfied that all recoveries have been made in respect of the banking institution, or considers that any remaining recoveries are sufficiently foreseeable so as to be included in the recoveries account on the date of the final notification, it shall calculate the net cost of resolution.

6. The net cost of resolution is the total amount in the expenses account less the total amount in the recoveries account on the date of the final notification, but if the total amount in the recoveries account equals or exceeds the total amount in the expenses account, the net cost of resolution is zero.

PART 2

Calculation of the scheme manager's limit

7. The Treasury shall create accounts of—

(a) notional net expenditure ("the notional account"), and

(b) actual net expenditure ("the actual account"),

of the scheme manager in respect of the banking institution.

8. The Treasury shall date the accounts as from the time when the scheme manager would have first, or has for the first time, incurred expenses or made recoveries under paragraphs 7(a) or (b).

9. At the time when—

(a) the scheme manager would have incurred expenses (as determined by the scheme manager under section 214D(2) of the Act), those amounts shall be added to the notional account;

(b) the valuer determined that the scheme would have made recoveries under section 214D(3), those amounts shall be subtracted from the notional account.

10. At the time when the scheme manager—

(a) incurred actual expenditure in respect of the banking institution, those amounts shall be added to the actual account;

(b) made recoveries in respect of the actual expenditure, those amounts shall be subtracted from the actual account.

11. In the notional account, the Treasury shall account for interest at the notified rate on the outstanding balance as if it had accrued daily and had been added to the account on each anniversary of the relevant time.

12. In the actual account, interest at the notified rate shall accrue daily on the outstanding balance and shall be added to the account on each anniversary of the relevant time.

13. In paragraphs 11 and 12, where the final notification is made on a date falling after an anniversary date, then all accrued interest not yet added shall be added to the account on the date of the final notification.

14. The scheme manager's limit is the outstanding balance in the notional account less the outstanding balance in the actual account on the date of the final notification.

PART 3

Calculation of the total cost of interim payments

15. The Treasury shall keep an account of any interim payments made by the scheme manager under regulation 9.

16. The account shall be dated from the time when the Treasury or the other person first received an interim payment.

17. The Treasury shall add the interim payments to the account on the date on which they are received.

18. Interest at the notified rate shall accrue daily on the amount in the account and shall be added to the account on each anniversary of the relevant time, but where the final notification is made on a date falling after an anniversary date, then all accrued interest not yet added shall be added to the account on the date of the final notification.

19. The total cost of interim payments is the total amount in the account on the date of the final notification.

PART 4

Calculation of balancing payments

20. A balancing payment is due—

(a) from the scheme manager if both the net cost of resolution and the scheme manager's limit exceed the total cost of interim payments; or

(b) from the Treasury to the scheme manager if either the net cost of resolution or the scheme manager's limit (or both) are lower than the total cost of interim payments.

21. If paragraph 20(a) applies, then the amount of the balancing payment shall be the lower of the net cost of resolution and the scheme manager's limit, minus the total cost of interim payments.

22. If paragraph 20(b) applies then the amount of the balancing payment shall be the total cost of interim payments less the lower of the net cost of resolution and the scheme manager's limit.

SCHEDULE 2

Regulation 13

PART 1

The valuer

1. The valuer is to hold and vacate office in accordance with the terms of his or her appointment.

2. The Treasury may remove the valuer only on the ground of incapacity or serious misbehaviour.

3. In the event of the death of the valuer, or if the valuer is removed from office or resigns, the Treasury (or a panel appointed by the Treasury) shall appoint a new valuer as soon as possible.

4. The valuer shall be—

(a) paid such remuneration, and

(b) reimbursed such expenses,

as the Treasury may determine.

5. The Treasury may appoint a person to verify the remuneration and expenses of the valuer.

6. The valuer may appoint staff.

7. The valuer shall determine the remuneration and other conditions of service of persons appointed under paragraph 6.

8. Any determination under paragraph 7 shall require the approval of the Treasury.

9. Valuers (and their staff) are neither servants nor agents of the Crown (and in particular are not civil servants).

10. Records of a valuer in relation to his or her functions in connection with an appointment under these Regulations are public records for the purposes of the Public Records Act 1958(**a**).

PART 2

Application to the court for information

11.—(1) The court may, on an application by the valuer, make an order requiring a person to provide information that is reasonably required for the purpose of making the determinations in section 214D(3).

(2) A person required to provide information pursuant to an order under sub-paragraph (1) shall not be required to provide information—

(a) in respect of which a claim to legal professional privilege (in Scotland, to confidentiality of communications) could be maintained in legal proceedings,

(b) if such provision by the person holding it would be prohibited by or under any enactment, or

(c) if it is held by a government department and provision of such information would be contrary to the public interest.

(3) In relation to information recorded otherwise than in legible form, the power to require it to be provided includes power to require it to be provided in a form from which it can be readily produced in visible and legible form.

(**a**) 1958 c.51.

12. A person who provides information to the valuer for the purpose set out in paragraph 11(1) is not, by reason only of the provision of such information, liable in any proceedings relating to a breach of confidence.

13. Specified information shall not be disclosed by the valuer (or any person to whom the valuer has disclosed such information in accordance with paragraph 14(2)) without the consent of the person from whom the valuer obtained the specified information and, if different, the person to whom it relates.

14.—(1) The prohibition in paragraph 13 of the disclosure of specified information is subject to the following exceptions.

(2) The valuer may, for the purpose of making the determinations under section 214D(3), disclose specified information to any staff appointed by the valuer or to any person providing advice or assistance to the valuer.

(3) The valuer may disclose specified information if and to the extent that the valuer considers it necessary to do so for the purposes of exercising the functions of the office.

(4) The valuer must, before disclosing any specified information in accordance with sub-paragraph (3), have regard to the need to exclude from disclosure (so far as practicable)—

(a) commercial information the disclosure of which might significantly harm the legitimate business interests of the person to whom it relates,

(b) information relating to the private affairs of an individual, the disclosure of which might significantly harm the individual's interests, or

(c) any information the disclosure of which would be contrary to the public interest.

(5) The valuer may disclose specified information in accordance with this paragraph subject to such conditions as the valuer thinks appropriate.

15. In this Part, "specified information" means any information obtained by the valuer for the purpose of making determinations under section 214D(3) of the Act.

SCHEDULE 3

Regulation 16

PART 1

Proceedings before Tribunal: general provision

1. This Part applies in the case of a reference to the Tribunal under regulation 14(5) or 15 in respect of—

(a) a reconsidered determination of the valuer under regulation 14;

(b) a determination of the scheme manager under section 214D(2); or

(c) a calculation made by the Treasury in connection with its functions under these Regulations.

2. This Part also applies in the case of a reference to the Tribunal under regulation 15 in respect of a dispute relating to the making of payments under these Regulations.

3. On receiving a reference described in paragraph 1—

(a) Tribunal Procedure Rules may make provision for the suspension of the determination or calculation to which the reference refers from taking effect;

(b) the Tribunal may consider any evidence relating to the subject matter of the reference, whether or not it was available to the person making the determination or the calculation at the material time.

4. On receiving a reference described in paragraph 1 or 2, the Tribunal must determine what (if any) is the appropriate action—

(a) in the case of a reference described in paragraph 1, for the person making the determination or calculation to take in relation to the matter referred to it (and that person must act in accordance with the determination of, and any direction given by, the Tribunal;) or

(b) in the case of a reference described in paragraph 2, to be taken to resolve the dispute, which may include an award of damages.

5. An award of damages under paragraph 4(b) may only be made if the Tribunal is satisfied that an award would have been made by a county court or, in Scotland, the Court of Session, if the claim had been made in an action begun in that court.

6. An order of the Tribunal or an award of damages may be enforced—

(a) as if it were an order of or award made by a county court; or

(b) in Scotland, as if it were an order or award made by the Court of Session.

PART 2

Offences

7. This Part applies in the case of proceedings before the Tribunal in respect of a reference described in paragraph 1(a).

8. A person is guilty of an offence if that person without reasonable excuse—

(a) refuses or fails—

(i) to attend following an issue of a summons by the Tribunal, or

(ii) to give evidence; or

(b) alters, suppresses, conceals or destroys, or refuses to produce a document which that person may be required to produce for the purposes of proceedings before the Tribunal.

9. A person guilty of an offence under paragraph 8(a) is liable on summary conviction to a fine not exceeding level 5 on the standard scale.

10. A person guilty of an offence under paragraph 8(b) is liable—

(a) on summary conviction to a fine not exceeding the statutory maximum;

(b) on conviction on indictment to imprisonment for a term not exceeding two years or a fine or both.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations are made under sections 214B and 214D of the Financial Services and Markets Act 2000 (2000 c.8) and provide for the Treasury to notify the Financial Services Compensation Scheme ("the scheme") if they require the scheme to contribute to expenses incurred in connection with the exercise of a stabilisation tool in respect of a banking institution under Part 1 of the Banking Act 2009 ("the 2009 Act").

Regulation 3 describes the expenses to which the Treasury may require the scheme to contribute.

Regulation 4 provides that where section 214B(2) applies, the Treasury may send the scheme manager an initial notification. This notification includes details of the banking institution and the

stabilisation power, sets out the expense incurred or expected to be incurred and whether or not a payment is required immediately from the scheme manager. The notification also sets out the interest rate to be applied to the accounts kept in respect of the resolution under Schedule 1.

Regulation 5 provides for the initial notification to be updated on the occurrence of certain events.

Regulation 6 provides for the scheme manager, on receipt of the initial notification, to make the determinations under section 214D(2) and to keep a record of its actual expenditure.

Regulation 7 provides that the Treasury shall keep the accounts set out in Part 1 of Schedule 1.

Regulation 8 provides that the Treasury, on receipt of information from the scheme manager and the valuer, shall determine the limit of the amount of special resolution regime payments the scheme manager can be required to make.

Regulation 9 applies where either the Treasury requires the scheme manager, or the scheme manager volunteers, to make an interim payment and provides that the Treasury shall establish the maximum amount of interim payment that can be made.

Regulation 10 provides for the final notification for payment where no interim payments have been made.

Regulation 11 provides for the final notification for payment where interim payments have been made.

Regulation 12 provides for the accounts kept in accordance with Schedule 1 and expenses included in those accounts to be independently verified.

Regulation 13 provides for Part 1 of Schedule 2 to apply to a valuer appointed by the Treasury under section 214D(3). It provides that the Treasury may specify principles for the valuer to apply and for the valuer to notify their determinations to the Treasury.

Regulation 14 provides for the scheme manager or the Treasury to require the valuer to reconsider their determinations and to make a reference to the Tribunal.

Regulation 15 provide for other disputes arising under the Regulations to be referred to the Tribunal.

Regulation 17 provides that payments made by the scheme manager under the Regulations are to be treated as payment of compensation to eligible claimants.

Regulation 18 makes transitional provision for notifications made under the Financial Services and Markets Act 2000 (Contribution to Costs of Special Resolution Regime) Regulations 2009 (S.I. 2009/ 807).

Schedule 1 provides for accounts to be kept to allow the Treasury to calculate the net cost of resolution, the scheme manager's limit, the total cost of interim payments and any balancing payments.

Schedule 2 provides for the valuer to hold office and to be remunerated and to apply to the court for information to be disclosed.

Schedule 3 makes provision for proceedings before the Tribunal under these Regulations and for offences in relation to these proceedings.

A full impact assessment of the effect that this instrument will have on the costs of business is available from [ ] and is annexed to the Explanatory Memorandum which is available alongside the instrument on the OPSI website.

HM Treasury contacts

This document can be found in full on our website at:
hm-treasury.gov.uk

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